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RESEARCH TOPIC

THE EXPORT LED GROWTH HYPOTHESIS: A SYNTHESIS FOR SERVICES EXPORT LED GROWTH FOR INDIA

(1995 TO 2015)

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RESEARCH GUIDE

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1. Introduction

It is widely accepted that economic growth is full of complexities and depend on many factors including trade. The export led growth hypothesis (ELGH) suggests that export expansion is one of the main determinants of economic growth. It also advocates that economic growth can also be enhanced by expanding exports along with other influential factor of growth. And thus exports can become an "engine of growth". The countries observe positive externalities for domestic economy by participating in world markets such as reallocation of existing factors, economies of scale and global competition. Though there are no theoretical or empirical studies which support the above positive externalities.

There have been proponents of trade, that trade benefit the nations involved in, like Adam Smith, Ricardo, Heckesher-Ohlin since nineteenth century and later many neo-classicists. And the country that has surplus balance of payments has more benefits to rip from the trade by allocating unused resources for additional revenue that contribute economic growth of the nation. And so having surplus exports is always preferred by the countries as it contributes to externalities to economic growth.

A number of empirical studies have documented a strong and positive relationship between export and economic growth including Emery (1967), Michaely (1977), Balassa (1978 and 1985), Heller & Porter (1978), Tyler (1981), Feder (1983), Kavoussi (1984), Jung & Marshall (1985), Ram (1985), Chow (1987), Darrat (1987), Grier & Tullock (1989), Fosu (1990), Kugler (1991), Ahmad & Kwan (1991), Sengupta (1991), Ekanayake (1999), McCarville and Nnadozie (1995), Thornton (1996) and Panas and

Vamvoukas (2002); the list is extensive. The export-led growth hypothesis has been evidential for various countries and also for group of countries. Many studies found unidirectional causal relationship from export to economic growth, whereas there are studies that observed unidirectional causation from output growth to export.

Gabriele A. (2004a) stated that services exports too have a positive impact on GDP growth in developing countries. Expanding service sector is not only helping the domestic economy but also having faster growth in services exports, mainly due to second generation reforms taken place in Indian economy in recent period. Treasury submission (2006) concludes that over the longer term, services have comprised an increasing share of Australian exports, just as they are an increasing share of total domestic production and employment.

Post second world war, there have been studies on inter sectoral shift in employment from agriculture to industry and industry to services which suggests that as per capita income rises the employment share of each sector observes transformation. Fisher (1935), Clark (1940), Kuznets (1973), Fuchs (1968), Gemmell (1982), Chenery and Taylor (1968), Boumol (1967) and Kothe (2012) have discussed not only pattern of change in inter sectoral shifts in employment but also observed the determinants for the same. Some argue that rising income makes people to demand more of the services, whereas others argue that inter sectoral productivity forces the shifts in employment shares. And it is also evident from many developed and developing countries that there have been shifts in employment shares as per capita income rises.

There is an impressive growth record since the then Finance Minister (and now Prime Minister) Manmohan Singh initiated key economic reforms in June 1991, resulting in reduced public sector participation in the economy, greater openness to international competition, and significant deregulation. Since those reforms, India's economic growth has averaged around six per cent, far ahead of its previous sluggish performance; and over the past three years growth has been of the order of 7.5 to 8.5 per cent. It is argued that India has experienced services revolution in recent past which led its share to reach to more than 65 per cent in GDP and 35 per cent in employment (Kothe, 2012).

It is believed that the growth in the service sector in India has been led by the IT–ITES sector, contributing substantially to increase in GDP, employment, and exports. The exports of IT and ITES have cemented the dominating existence of India's trade in services in the world (Kothe, 2015). Further while observing the external determinants of services exports, Kothe (2014) initiated measurement of price and income elasticities that have caused substantial increase in India's services exports.

There is a great advantage in exports being led by services. While integration with the global supply chain through the manufacturing exports route subjects a country to high risk for even mild cyclical fluctuations, services sector could more easily withstand shocks and target potential export destination bases.

2. Need of Research

Now in recent period, services exports in India has experienced substantial flow and have generated a large pool of employment within the economy. Largely, services exports that were earlier limited to remittances for labours employed outside the country, now have

rose many folds due to the changes in the characteristics of services that are traded internationally that include storability, simultaneity of production and consumption and separability in location. It is observed that the liberalization and globalization have caused for emergence of modern services in transport, communication, financial, banking, media and R&D sectors. Due to ICT driven digitalization and automation also have created export potential for India being one of the giants in software development in world.

The information technology and communication revolution along with services that are serving world through BPOs have changed the nature, composition and trends of overall exports of India. Additionally, tourism has also contributed positively in overall services exports. Ultimately that have boosted the domestic employment serving domestic economy and also the world markets along with existing employment in traditional sectors. Hence it indicates that services exports have positively influenced not only economic growth within the country but also economic development.

India's labour force is younger, better nourished and has more skills than before. Clearly India's labour force is undergoing rapid structural transformation: the proportion of the working population is rising; the labour force is less nutritionally deprived and increasingly literate. These changes imply substantial quality improvements in the Indian labour force. Economic theory and international experience leads us to believe that this will lead to sharp rises in labour productivity and an upward shift in the trend long run rate of growth of the Indian economy.

Development theory usually identifies three stages of development, the 1st stage when the primary sector is the dominant sector in GDP, the second stage in which manufacturing is dominant and the third stage in which the tertiary sector is dominant and is identified with countries in an advanced stage of development. India's growth experience does not seem to follow this theory of stages as the high growth and high share of services sector which is a feature of a developed economy has been attained by India even before reaching a developed stage. Rather than debating on which growth strategy is ideal, it is important to realise that the constraints in the industrial and agricultural sectors and the natural advantage of India in services sector has led to a services led growth of the economy. While the constraints in the other two sectors need to be removed as is being attempted now, there is no need to expect the hare to sleep for the tortoise to overtake it. There is in fact a need to tap our full potential in the services sector. The services sector is central to the national strategy to re-engineer the economy to focus on domestic sources of growth (Kanapathy 2003).

Services sector growth can also complement growth in manufacturing sector. There are sectors where a lot of complementary exists between services & manufacturing growth e.g. Telecom Services and Telecom equipment manufacturing, electronic hardware & software where a hardware-software combination can accelerate growth of both hardware and software as suggested in the Medium Term Export Strategy (MTES) of the Department of Commerce, healthcare services and pharmaceutical sector, shipbuilding along with ship repair & maintenance services and shipping where growth is sure with growth in volume of trade, R&D services and pharma & biotech sectors, etc. Identifying and promoting the growth of these sectors with considerable backward – forward

linkages can help growth of both services and manufacturing and some manufacturing sub-sectors can ride piggy back on the success of the complementary services to achieve quick growth.

Thus the services sector has high potential. Till now, we have been focusing mainly on software. We have many such niche sectors in services. The recent growth in export of professional services is an example of the potential of other services.

Foreign trade plays a vital role in the economic development of a country. It is a primary link of integration with the other world economies. India is no exception to it and being a developing economy, the foreign trade has long lasting ramifications on the economic health of the country. In recent times of slowdown across global economies, India is considered to be one of the most exciting markets for foreign trade with a large base of export and import centric industries. Considering the merchandise trade, India's share in total world exports is 1.6% while that of imports is 2.4%. On the other hand, the share of services exports in the world is 3.2% and that of imports is 3.0%.

During the last few decades, trade in services has emerged as the major contributor to the better economic performance of India. Services sector contributes about 55% to the country's GDP. However, this sector contracted amidst adverse global economic situations. India's trade in services also indicated contraction as has been registered by merchandise trade. The net trade in services has slid by 5.61% y-o-y in 2015-16, from $68.26 bn to $64.43 bn. The receipts from services fell by $4.08 bn compared to same period last year, showing a decrease by 2.79%. The payments or imports eased by 0.32%, a fall by $250 mn. There is increase in merchandised exports by 4 times and services

exports increased by more than 7 times during the last decade and half. This implicates some research problems, what is the contribution of services in exports since 1995-96? Is there any correlation between growth of services sector and growth of exports? What is relative share of sub sectors in services exports? Are there any assistance and policy measures required to sustain growth of services exports?

There is neither substantial literature that advocates services exports led growth model for economic growth for any country in the world nor for India. And hence it is needed to analyze the nature, composition and trends in services exports and also to observe determinants for economic growth in the context of export led growth hypothesis with special reference to services exports in India. The present study is an attempt to formulate a services export led growth model for the developing countries that have large portion of unemployed work force. And also to suggest measures to sustain growth in India's services exports that largely influence overall economic growth.

This study will provide an opportunity for having a closer look at the services exports of the country. An attempt will be made to expose the truth relating to growing services exports of the country. The limited literature on the theme also encouraged interest for the attempt of thorough study of the services exports of the country. The study is intended to bring out the various facets of India's services exports.

The study would evaluate the contribution of services in exports since 1995-96. There would be an attempt to correlate growth of services sector and growth of exports. The study would addresse the relative share of sub sectors in services exports. There would be an endeavor to formulate a model of services export led growth for sustainable

development which also would help in formulation of policy measures required to sustain growth of services exports.

3. Objectives of the study

- To assess the contribution of services sector in gross domestic product in India since 1996.
- To evaluate the share of services in exports of the country.
- To find the relationship between growth of services sector and growth of exports.
- To study the factors affecting services exports.
- To evaluate the need of increase in services exports.
- To study existing initiatives by the Govt. to increase the services exports.
- To suggest the measures to increase the services exports in the economy.
- To formulate Services Export Led Growth Model (SELGM) for Developing Countries.

4. Hypothesis

1. There has been significant increase in the contribution of Services sector to GDP in India.
2. Services exports has pivotal role in overall exports of the country.
3. There is significant relationship between growth of services and growth of overall exports.
4. Economic factors have significant impact over services exports.

5. The increase in services exports is due to the policy initiatives undertaken by the Govt. of India.
6. There has been causal relationship between services exports and economic growth in recent period in the context of Indian economy.
7. SELG Model would be a successful model for economic growth in developing countries.

5. Data and Research Methodology

There would be use of mainly secondary data for the present study.

- The reports published by Govt. and related organizations which includes Central Statistical Organisation, Ministry of Finance, Reserve bank of India, UNCTAD and World Bank.
- Books
- Articles and Research Papers published in National and International Journals
- The information from the Govt. literature.

There will be use of statistical and econometrical design. Econometrics methodologies like Regression (OLS), Time series analysis, Granger causality (1987), VAR (1987 and 1991) and VECM (1990) would be applied which incorporates all types of required tests including stationarity (Dickey-Fuller, 1979 and 1981). There would be further use of relevant statistical and econometric tools in the study.

6. Scope and Significance of the Study

In the new wave of globalization, due to trade liberalisation, there has been increase in relevance of services trade instead of trade in goods in most of the economies in the world. The developing economies need to face global competition efficiently in the long run and to grow significantly, holding inefficient services sector.

There have been significant structural changes in Indian economy since the inception of New Industrial Policy, 1991. The formation of WTO incorporated to new opportunities in global trade in goods and services since 1995. India, among the BRICK nations, has been benefitted at large extent to have further increase in trade in services during 1996 to 2015. There is need of evaluate the services exports and its relevance in economic growth in relation to Indian economy for the period of 1996 to 2015.

7. Chapter Plan

The chapter plan for the present study is as follows.

1 Introduction

2 2.1 Research Problem

2.2 Scope of the Study

2.3 Selection of Research Problem

2.4 Significance of the Study

2.5 Objectives of the Research

2.6 Hypothesis

2.7 Literature Review

2.8 Research Methodology

2.9 Limitations

3 Concepts and Definitions

4 Services Sector and Development Theories

5 Contribution of Services Sector to GDP

6 India's Services Exports Scenario in Pre-Planning Period

7 Services Exports during 1950-51 to 1994-95

7 Services Exports for the period of 1995-96 to 2006-07

8 Services Exports and Economic Growth

9 India's Sub-Services Exports (1995-96 to 2006-07)

9.1 Exports of Travel Services

9.2 Exports of Transportation

9.3 Exports of Insurance Services

9.4 Exports of G.N.I.E.

9.5 Exports of Miscellaneous Services

9.5.1 Exports of Software Services

9.5.2 Exports of Business Services

9.5.3 Exports of Financial Services

9.5.4 Exports of Telecommunications Services

10 The Services Export Led Growth Model for developing countries.

11 Conclusion

12 Bibliography

12 Annexures

8. Limitations

The study is an attempt to develop a SELG Model for India which may be strictly useful for developing countries like India. It considers only data from 1995 to 2015 which may further can generate some different results in other cases. It mainly would be based on secondary data provided by the competent authorities so results solely depending upon the validity of the data.

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